

11 U.S.C. § 507(a)(8)(D)  
11 U.S.C. § 507(a)(8)(E)  
ORS Ch. 657 et. seq.  
ORS 657.505(7)(a)  
Tax

In Re Cottage Grove Hospital

Case # 698-64406-aer11

2/6/01

Radcliffe

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Oregon's Unemployment Compensation Trust Fund is a statutory fund out of which unemployment benefits are paid to displaced workers. It is funded by employer contributions, normally as a percentage of payroll. Instead of making these percentage payments, Debtor, as a nonprofit employer, elected to reimburse the fund for unemployment benefits paid.

A priority claim for unpaid reimbursement obligations was filed by the Oregon Employment Department in Debtor's Chapter 11 case. Debtor objected. The issue at bar was whether the obligation to reimburse constituted a priority "tax" under § 507(a)(8). The Court held it did under the multi-pronged analysis set out in In Re Lorber Industries of California, 675 F.2d 1062 (9<sup>th</sup> Cir. 1982) and its progeny. The court did not reach the issue of whether the taxes were "employment" taxes under § 507(a)(8)(D) or excise taxes under § 507(a)(8)(E).

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UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF OREGON

In Re:	)	Bankruptcy Case No.
	)	698-64406-aer11
COTTAGE GROVE HOSPITAL, an	)	
Oregon non-profit corporation,	)	MEMORANDUM OPINION
	)	
Debtor.	)	

This matter comes before the court on the objection of the Reorganized Debtor (Debtor) to the claim of Oregon Employment Department (OED). The sole question is whether the OED's claim for reimbursement of unemployment benefits is a priority tax within the purview of 11 U.S.C. § 507(a)(8).<sup>1</sup> Before considering the facts in this case, an overview of Oregon's unemployment compensation scheme and employers' contributions thereto is in order.

Oregon's Unemployment Compensation Trust Fund:

Oregon has established a statutory scheme to provide benefits to unemployed workers. See ORS Ch. 657. In general, employees who have been laid off from their regular employment, but who remain

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<sup>1</sup>Unless otherwise noted, all subsequent statutory references are to Title 11 of the United States Code.

1 available for work and actively seek employment are entitled to  
2 benefits. See ORS 657.155. All Oregon employers, with exceptions  
3 and exemptions not relevant here, pay into the Unemployment  
4 Compensation Trust Fund (the Fund) to provide for the benefit of  
5 unemployed workers. Oregon law denominates such payments as  
6 "taxes". ORS 657.505(1). The Fund is administered by the OED.  
7 Payments are to be made quarterly. They are a percentage of payroll  
8 (percentage payments). The percentages are based on an employer's  
9 experience with respect to benefits paid from the Fund. See, ORS  
10 657.430; ORS 657.435; and ORS 657.462.

11 In lieu of the percentage payments, nonprofit employers may  
12 elect to reimburse the Fund by making reimbursement payments as  
13 described in ORS 657.505(7)(a).<sup>2</sup> Like percentage payments, Oregon  
14 law denominates reimbursement payments as "taxes". Id.<sup>3</sup> Within  
15 thirty (30) days of the effective date of its election, the  
16 nonprofit employer must post security with the OED's director. ORS  
17 657.505(7)(d). One type of allowable security is a surety bond.  
18 Id.<sup>4</sup>

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20 <sup>2</sup> ORS 657.505(7)(a) provides in pertinent part:  
21 [S]uch nonprofit employing unit may elect to make  
22 reimbursement payments into the Unemployment Compensation  
23 Trust Fund in an amount equivalent to the amount of  
24 regular benefits and one-half of extended benefits paid  
25 out to claimants who during the applicable base period  
26 were paid wages by such nonprofit employing unit.

27 <sup>3</sup> The election to make reimbursement payments is made by written notice, is  
28 good for two years, and is cancelable. ORS 657.505(7)(b) & (c).

29 <sup>4</sup> The bond amount is determined as a percentage of the employer's total  
30 wages paid for covered employment for the four (4) calendar quarters immediately  
31 preceding the effective date of the election. ORS 657.505(7)(d). The  
32 (continued...)

1 ORS 657.505(8) (a), provides in pertinent part:

2 "At the end of each calendar quarter, . . . the  
3 director shall determine the amount of payments in  
4 lieu of taxes or reimbursement payments required under  
5 subsections (5), (6) and (7) of this section, and  
6 shall bill each employer for such amount."

7 Payment of any bill rendered under paragraph (a)  
8 of this subsection shall be made not later than the  
9 last day of the month immediately following the month  
10 in which such bill was mailed to the last known  
11 address of the employer or was otherwise delivered to  
12 it. The director may assess a nonprofit employing  
13 unit for past due taxes and such assessment shall be  
14 subject to the same interest, penalties, enforcement,  
15 appeal and any other provisions of this chapter that  
16 apply to taxes assess pursuant to ORS 657.681.

17 ORS 657.505(8) (c) .

18 The Fund must be kept at adequate funding levels as  
19 determined by the director. ORS 657.459. This funding level  
20 determines an employer's percentage payment, ORS 657.462, and takes  
21 into account the amount of reimbursement payments owed. ORS  
22 657.467. Reimbursement payments are included in the Fund and in any  
23 computation of the Fund's adequacy. Id. There is no private or  
24 self unemployment insurance option available in Oregon.

25 Facts:

26 The facts are undisputed. Debtor was a nonprofit employer  
which, in February, 1977, filed a Notice of Election to Reimburse in  
Lieu of Taxes, and consequently posted a surety bond. The election

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<sup>4</sup>(...continued)  
percentages are set by statute. Id. The bond must be in force for at least two  
(2) years and is subject to adjustment by the director. ORS 657.505(7) (d) (A) .

1 was never canceled. As a result of financial difficulties, debtor  
2 laid off many employees. They filed claims for unemployment  
3 benefits, which the OED paid pursuant to the statutory scheme  
4 described above.

5 Debtor filed its Chapter 11 petition on July 27, 1998. Its  
6 amended plan was confirmed by an order entered on June 29, 1999.

7 At the time this matter was taken under advisement, the OED  
8 had filed an amended priority proof of claim in the sum of  
9 \$436,576.73 for unpaid reimbursement payments. The claim amount  
10 reflected a \$53,762.00 credit in May, 1999, from payment by Debtor's  
11 surety. Debtor did not dispute the claim amount.<sup>5</sup>

12 Discussion:

13 The only dispute is the classification of the unpaid  
14 reimbursement payments. The OED argues they are either "employment"  
15 or "excise" taxes under §§ 507(a)(8)(D) or (E).<sup>6</sup> Debtor argues they

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17 <sup>5</sup>After this matter was taken under advisement, the OED amended its proof of  
18 claim seeking additional unpaid reimbursement payments. Since this opinion deals  
19 solely with the priority to be accorded to the OED claim, no attempt is made to  
determine any dispute which may exist concerning any additional amounts sought by  
the OED.

20 <sup>6</sup> Sections 507(a)(8)(D) & (E) provide, in relevant part, as follows:

21 a) The following expenses and claims have priority in the following order:  
22 (8) Eighth, allowed unsecured claims of governmental units, only to  
the extent that such claims are for--

23 (D) an employment tax on a wage, salary, or commission of a  
24 kind specified in paragraph (3) of this subsection earned from  
25 the debtor before the date of the filing of the petition,  
whether or not actually paid before such date, for which a  
return is last due, under applicable law or under any  
extension, after three years before the date of the filing of  
the petition;

26 (continued...)

1 are more in the nature of a contractual obligation, thus, OED's  
2 claim is not entitled to priority and should be allowed only as a  
3 general, unsecured claim.

4 This appears to be a case of first impression in this  
5 district. In general, whether an obligation qualifies as a tax for  
6 §507 purposes is a federal question. In Re Arrow Transportation  
7 Co., 229 B.R. 456 (D. Or. 1999). This Court is not bound by state  
8 law labels. Instead, it must look at the characteristics of the  
9 debt. Id. In In re Lorber Industries of California, 675 F.2d 1062  
10 (9th Cir. 1982), the court described a tax<sup>7</sup> as:

11  
12 <sup>6</sup>(...continued)

(E) an excise tax on--

13 (i) a transaction occurring before the date of the  
14 filing of the petition for which a return, if required,  
15 is last due, under applicable law or under any extension,  
16 after three years before the date of the filing of the  
petition; or

(ii) if a return is not required, a transaction  
occurring during the three years immediately preceding  
the date of the filing of the petition.

17 There is no dispute that the reimbursement payments at bar fall within the  
18 three (3) year reachback period of either subsection.

19 <sup>7</sup> On the other hand, a fee:

20 'is incident to a voluntary act, e.g., a  
21 request that a public agency permit an  
22 applicant to practice law or medicine or  
23 construct a house or run a broadcast station.

24 The public agency performing these services  
25 normally may exact a fee for a grant which,  
26 presumably bestows a benefit on the applicant  
not shared by other members of society.'  
National Cable Television Assn., Inc. v.  
United States, 415 U.S. 336, 340-341, 94  
S.Ct. 1146, 1149, 39 L.Ed.2d 370 (1974).

The chief distinction between a "tax"  
and a "fee" is that a tax 'is an exaction

(continued...)

- 1 (a) An involuntary pecuniary burden, regardless of  
2 name, laid upon individuals or property;  
3 (b) Imposed by, or under authority of the legislature;  
4 (c) For public purposes, including the purposes of  
defraying expenses of government or undertakings  
authorized by it;  
(d) Under the police or taxing power of the state.

5 Id. at 1066 (quoting In re Farmers Frozen Food Company, 221  
6 F.Supp.385, 387 (N.D.Cal 1963)).

7 Debtor argues that the first and third prongs have not been  
8 met. It maintains that the reimbursement obligation was voluntarily  
9 incurred when Debtor made the election to reimburse, thus, the  
10 payments are not an involuntary pecuniary burden.

11 The 9<sup>th</sup> Circuit has concentrated its voluntariness analysis on  
12 the source of the obligation. If the obligation was created by a  
13 voluntary act, such as using a sewer system, whereby user fees were  
14 consequent thereto, then the burden is voluntary and in the nature  
15 of a contract or fee. Lorber, supra. If, however, the obligation  
16 arose by legislative fiat, such as a noncomplying employer's  
17 statutory obligation to reimburse a worker's compensation fund, then  
18 the burden is involuntary. In Re Camilli, 94 F.3d 1330 (9<sup>th</sup> Cir.  
19 1996).

20 In In Re Sacred Heart Hospital of Norristown, 209 B.R. 650  
21 (E.D. Pa. 1997), the court construed the obligation to make

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23 <sup>7</sup>(...continued)  
24 for a public purpose, while a fee relates  
25 to an individual privilege or benefit to  
the payer.' U.S. v. River Coal Co., Inc.,  
748 F.2d 1103, 1106 (6th Cir.1984).

26 In Re Dawson, 98 B.R. 519, 522 (Bankr. D. Or. 1989).

1 reimbursement payments under the analogous Pennsylvania  
2 unemployment compensation laws. The court held the payments to be  
3 "involuntary". This Court agrees. Oregon's statutory scheme  
4 obligates an employer to pay into the Fund. Nonprofit institutions  
5 have two choices as to the form of payment, but they must pay  
6 nonetheless. Had Debtor not made the election to make reimbursement  
7 payments, it would have been required to make percentage payments.<sup>8</sup>  
8 See also, In Re Boston Regional Medical Center, 256 B.R. 212 (Bankr.  
9 D. Mass. 2000) (construing the analogous Massachusetts scheme).<sup>9</sup>

10 Further, it has been held that in the context of "excise"  
11 taxes, the "voluntariness" prong is a red herring, and is, in  
12 essence, inapplicable. In Re Arrow Transportation Co., 229 B.R. 456  
13 (D. Or. 1999).<sup>10</sup>

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15 <sup>8</sup> It is noteworthy that courts appear unanimous in holding that "percentage  
16 payments" in analogous state schemes are "taxes". See e.g., In Re Continental  
17 Minerals Corp., 132 B.R. 757 (Bankr. D. Nev. 1991) (Nevada); In Re Skjonsby Truck  
18 Line, Inc., 39 B.R. 971 (Bankr. D.N.D. 1984) (North Dakota); In Re Garden Inn  
19 Steak House, Inc. 22 B.R. 830 (Bankr. N.D. Oh. 1982) (Ohio). It would be anomalous  
to hold percentage payments involuntary, (and thus taxes), yet reimbursement  
payments "voluntary", when both fund the same benefit scheme, especially when  
reimbursement payments are included in determining adequate funding levels. See,  
ORS 657.467.

20 <sup>9</sup> In Boston Regional, the court performed the multi-factor "tax" analysis  
21 discussed above and below, concluding reimbursement payments under the  
22 Massachusetts scheme were "taxes" for bankruptcy purposes. It went on to hold  
23 however that these taxes were not "employment" taxes under § 507(a)(8)(D) and thus  
24 not entitled to priority. There, the state did not argue the payments were  
alternatively "excise" taxes under § 507(a)(8)(E). Here, OED has made such an  
alternative argument, and Debtor has only challenged the threshold determination  
of whether the reimbursement payments are "taxes" at all. As such, this court  
need not reach the issue of whether the payments are "employment" or "excise"  
taxes.

25 <sup>10</sup> "An excise tax is a 'tax imposed on the performance of an act, the  
26 engaging in an occupation, or the enjoyment of a privilege.'" Arrow, supra at 458  
(quoting Black's Law Dictionary, p. 506 (5<sup>th</sup> Ed. 1979)).



1 As to prong #3 (the public purpose requirement), it is  
2 axiomatic that Oregon's unemployment compensation scheme is for a  
3 public purpose, that is, aiding displaced workers, and hence the  
4 public in general. Some courts, notably the 6<sup>th</sup> Circuit Court of  
5 Appeals in two cases involving the same debtor, In Re Suburban Motor  
6 Freight, Inc., 998 F.2d 338 (6<sup>th</sup> Cir. 1993) (Suburban I); In Re  
7 Suburban Motor Freight, Inc., 36 F.3d 484 (6<sup>th</sup> Cir. 1994) (Suburban  
8 II), have refined the "public purpose" prong to further require  
9 that: 1) the pecuniary obligation be universally applicable to  
10 similarly situated entities; and 2) according the obligation  
11 priority treatment would not disadvantage private creditors with  
12 like claims. The 9<sup>th</sup> Circuit has not formally adopted the 6<sup>th</sup>  
13 Circuit's test, although it discussed and applied it in Camilli,  
14 supra, noting that since the Suburban criteria were met, it need not  
15 decide whether they were required in all cases.

16 Here, applying the Suburban criteria, payment into the Fund  
17 is universally required of all subject employers, that is, the state  
18 scheme is monopolistic. Sacred Heart, supra. Further, electing  
19 nonprofits are universally required to pay reimbursement payments.  
20 That there are several allowable forms of security does not change  
21 the universality of the obligation to reimburse.

22 As to disadvantaged private creditors with "like" claims, the  
23 only possible one would be the surety,<sup>11</sup> with a subrogation claim

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25 <sup>11</sup> The Court disagrees with Debtor's argument that Debtor's former  
26 employee's claims, based on unpaid personal benefit time are also "like" claims.  
Unpaid wages or benefits do not equate to unpaid obligations to Oregon's  
(continued...)

1 for amounts paid to the OED on the bond.<sup>12</sup> In Suburban II, the  
2 court did find that a surety, in the worker's compensation context,  
3 had a like claim on a bond posted by a self-insured employer.<sup>13</sup> In  
4 Sacred Heart, supra, the Court acknowledged some "likeness" of a  
5 surety's claim, but concluded the "other tax-like attributes . . .  
6 outweigh this single 'non-tax' characteristic." Id. at 658. To hold  
7 otherwise, would make the "tax" status of reimbursement payments  
8 dependent on whether subrogation rights had attached to the  
9 security posted for the payment. No sound policy supports this  
10 distinction.<sup>14</sup>

11 Further, the requirement imposed upon employers, under Oregon  
12 law, to make percentage payments or reimbursement payments to the  
13 Fund is analogous to the requirements imposed upon employers to make  
14 payments under the Oregon Workers' Compensation Law to aid injured  
15 workers (see ORS Ch. 656). The 9<sup>th</sup> Circuit has already held that  
16 the duty of a non-complying employer to reimburse the state for  
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18 <sup>11</sup>(...continued)  
19 unemployment compensation system. The former is a contractual obligation to  
20 compensate for individual benefits, the latter, a statutory obligation to a  
designated fund to spread the risk of displaced workers statewide.

21 <sup>12</sup> In Oregon, a surety, as well as the issuer of a letter of credit, has the  
right of subrogation. In Re XTI Xonix Technologoes, Inc., 156 B.R. 821 (Bankr. D.  
Or. 1993) (surety); ORS 75.1170 (issuer).

22 <sup>13</sup> OED argues the surety's claim is not similar in that its rights derive  
23 from a contract with the Debtor for which it received consideration. Also, it  
24 provided no benefits to displaced workers. However, "[s]ubrogation is a doctrine  
of exact substitution, upon which the subrogee acquires the position, rights and  
25 liabilities of the subrogor." Rusher v. Bunker, 99 Or. App. 303, 311, 782 P.2d  
170, 175 (1989).

26 <sup>14</sup> In fact, Congress may have set its policy regarding subrogees in the  
priority claim context. Under § 507(d), they are denied priority status.

1 workers' compensation benefits paid to an injured employee are in  
2 the nature of an excise tax. In re Camilli, 94 F.3d 1330 (9<sup>th</sup> Cir.  
3 1996). No sound public policy would support a determination that  
4 payments required under Oregon's Workers' Compensation laws are  
5 "taxes", while payments required to be made to the Fund do not have  
6 such priority.

7 Conclusion:

8 Whether denominated "employment" or "excise", the unpaid  
9 reimbursement payments at issue here are priority taxes under 11  
10 U.S.C. 507(a)(8)(D) or (E). Debtor's objection is overruled. A  
11 separate Order shall be entered.

12 This opinion constitutes the Court's findings of fact and  
13 conclusions of law; they shall not be separately stated.

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16 ALBERT E. RADCLIFFE  
17 Chief Bankruptcy Judge  
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